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SECTOR

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Sensitive but unclassified, entire text.

This is the second in a series of four cables examining the effect of U.S. migration and remittances on the economy of rural Mexico.

¶1. (SBU) Summary. Despite record amounts of remittances flowing from the U.S. to rural Mexico, sustainable economic development in those regions has been largely elusive. One factor inhibiting productive investment of remittances has been a scarcity of reliable financial services in rural areas which receive the majority of transfers. Although financial organizations in Mexico, including credit union chains and traditional banks, are expanding their coverage and range of services, there are still a number of economic and societal challenges limiting the effectiveness of these institutions. According to Antonio Carranza of the government development bank, (Bansefi), only 33% of the banking-aged population utilizes saving or investment services, thus hampering the positive long-term effects of the remittance flow into Mexico. End summary.

THE EXPLODING FINANCIAL TRANSFER MARKET

¶2. (SBU) According to the Bank of Mexico, in 2005 remittances from migrants in the U.S. totaled 20 billion dollars, second only to oil revenues (31.7 billion dollars) and nearly double the value of tourism income (10.7 billion dollars). Representing an increase of 17 percent compared to 2004 (16.6 billion dollars), this economic explosion is showing no sign of slowing. According to Eduardo Gonzalez, an economist for Banamex, remittance income in the month of January, 2006 was estimated to have risen by 27 percent over the same time period January 2005, from 972 million dollars to 1.582 billion dollars. The state of Michoacan, a predominantly rural state with an agrarian economy, saw on an annual basis an increase in 2005 of 399 million dollars to 2.594 billion dollars, 13 percent of the national total (though Michoacan accounts for less than 4% of the total population). Carlos Garcia, Director of Migrant Services for the state of Michoacan, estimated that 1.3 million Michoacanos currently reside in the U.S., most of whom transfer funds home on a regular basis.

¶3. (SBU) Supporting this growth is a booming money transfer industry. According to data provided by a Mexican Chamber of Deputies (lower house of Congress) study in December 2004,

from 1995-2004 the proportion of electronic transfers (as opposed to money orders or cash deliveries) increased from 60 to 91 percent. As the sector has grown, it has also diversified and fees have decreased. In 1995 the industry was dominated by Western Union and MoneyGram, but by 2004 increased competition among money transfer organizations (MTOs), along with market entry by banks and credit unions, resulted in the average transfer fee falling from 18 percent in 1995 to 4.4 percent in 2005 (according to Juan Lavallo, National Director of Remittances for HSBC bank). However, the participation rate of banks and credit unions in the money transfer industry is still estimated to be less than 5 percent, according to Manuel Orozco of Georgetown University.

The increased participation of banks and credit unions in this sector could be a key development in ensuring low-cost, convenient transactions for low-income customers in the near future.

THE POPULAR SAVINGS AND CREDIT LAW

14. (SBU) Credit unions (cooperatives) have existed in Mexico for over 50 years, but underwent massive restructuring mandated by the Popular Savings and Credit Law of 2001 (PSCL). The PSCL was passed as a response to the closings of numerous credit unions in 1999-2000 due to poor management and malfeasance, resulting in the loss of many members' savings and a subsequent distrust of these organizations. The PSCL requires that all non-bank financial institutions that plan to offer savings accounts conform with a rigorous standard of internal controls, a benchmark that has been met by only a handful of the 650 credit union chains which existed prior to 2001, according to Mario Gallarraga, Project Director for the World Council of Credit Unions (WOCCU).

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15. (SBU) While the largest credit union chains, such as Caja Popular Mexicana and Caja Libertad, are now licensed to offer standard services, five years after the passing of PSCL, the resulting scarcity of accredited chains has left many unserved, rural areas. Ironically, many of these communities are most dependent on remittance income (in some cases comprising 60-70 percent of the local economy), leaving many residents no option but to utilize higher-cost money transfer companies such as DineroExpress (which also do not offer savings accounts and credit services). Although Yolanda Luna, an assistant director for the National Savings Bank, told Econoff that the number of credit union members nationwide has increased to 3.5 million (from 2.0 million in 2004), additional branches of licensed cooperatives will be necessary to ensure financial services in underdeveloped areas.

CAJA POPULAR MEXICANA AND COOPERATIVES

16. (SBU) An example of the growing influence and scope of cooperative financial institutions in rural Mexico, Caja Popular Mexicana (CPM) is Mexico's largest and oldest credit union, with assets of over 1.2 billion dollars and 327 branches in 22 states, according to Galarraga. Supported by USAID since 1999, and WOCCU since 2001, CPM has demonstrated strong growth, increasing its average rate of growth from 980 members/month in 2001 to 12,200 members per month in 2006. A central challenge faced by any credit union chain seeking to offer remittance services is establishing the systems infrastructure to transfer the funds as well as having the bargaining power to negotiate an agreement with a major MTO in the U.S. CPM has had an agreement with Vigo, a company with substantial experience with the Latin American remittance market as well as branches conveniently located in areas with large Mexican migrant populations in the U.S. since 2003.

17. (SBU) A key factor in its success, CPM possesses a

sophisticated information technology system called IRnet, which is provided to all credit unions who work with WOCCU, and is also utilized by Mexico's second-largest credit union, Caja Libertad. According to Luis Ortiz, a CPM branch manager in Pastor Ortiz, a small farming community in Michoacan, the number of remittances processed by CPM's remittance service, Pagomex, increased from 2,921 transfers in 2003 to 142,567 in 2005. This pace is showing no signs of diminishing, with 25,833 transactions made in the first two months of 2006 alone. However, although CPM has aggressively marketed Pagomex in Mexico, Pagomex is still virtually unknown in the U.S.

18. (SBU) CPM faces formidable competition from other credit unions as well as national banks in larger communities. While credit unions generally do not yet offer many of the services banks do, such as ATMs, internet banking, and credit cards, Santiago Alvarez, branch manager in Puruandiro, a larger agricultural community of 70,000 located 60 miles west of Morelia in the state of Michoacan, explained to Econoff that CPM's competitive advantage versus the larger banks was the non-intimidating, personal service provided by their employees. Puruandiro is an exception due to the presence of Bancomer and HSBC branches, although Alvarez estimated that only 5 percent of local residents are bank customers, while the 18 credit unions capture the majority of business.

19. (SBU) In contrast to the commercial banks (Bancomer and HSBC) located on the central plaza, the CPM in Puruandiro was opened on a side street next to the bustling fruit and vegetable market. In some ways, the branch looks like a garage, lacking a door but having an inviting atmosphere. Clients who regularly receive remittances there attested to Econoff that their previous distrust of financial institutions had been overcome by the friendly, helpful atmosphere of the company. One customer, Maria Ramirez Arriaga, stated that "I am a poor person, and of course we don't use banks, who only steal from us anyway. However, Caja Popular Mexicana has treated us with respect." Ramirez went on to mention that since becoming a member, she had applied and qualified for a loan based on the remittance income she receives from her sons, which she used to purchase an additional tractor. Other clients cited lower fees (compared to banks) as the primary reason for their loyalty.

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The lack of certain services offered by banks did not appear to be a detriment to most rural customers, many of whom now have access to financial services for the first time. Marketing credit products to previously un-banked customers appears to be an important key for credit union profitability, given the low money transfer profit margins.

110. (SBU) There has also been a change in the perception of the credit-worthiness of remittance recipients. While historically wire transfers (even those sent on a regular basis) were not considered dependable indicators of solvency, today clients of cooperatives such as Ramirez can obtain credit based solely upon remittance income. The new ability of many people to obtain loan products from credit unions may significantly boost productive economic activity in many rural areas, and illustrates a major difference between cooperatives and traditional banks.

THE NATIONAL SAVINGS BANK

111. (SBU) Created by the Popular Savings and Credit Law, Bansefi serves as a second-tier bank designed to offer savings accounts to the unbanked population as well as to strengthen a network of smaller credit unions across the country. Authorized by the federal government to create a national remittance delivery network in 2003, it developed "La Red de la Gente" (The People's Network), which has negotiated agreements with 10 money transfer organizations

(MTO) including MoneyGram, Vigo, and USBank. "La Red de la Gente" has been marketed heavily by Bansefi, utilizing former migrant stars such as Andres Bermudez (The Tomato King) as spokespeople. Presently, La Red includes over 750 branch offices, many of whom are small chains of only one or several branches and would have little or no chance of negotiating agreements with U.S.-based MTOs. Antonio Carrasco, National Director of La Red, explained to Econoff that Bansefi is aggressively pursuing agreements with large national banks and credit unions in the U.S. in order to expand the reach and capabilities of La Red. Carrasco and his colleagues, Yolanda del Rosario and Jaime Reynosa, fervently described their desire to include not only banks but universities, governmental institutions, and even the U.S. Embassy in the network in the future.

¶12. (SBU) Although Bansefi enjoys the advantages of being promoted by the Ministry of the Economy, a distinct product (La Red) and brand name, and a single-minded philosophy ("bank the un-banked"), it has suffered setbacks in its attempt to create additional financial opportunities for Mexico's poor. One problem is that Bansefi does not allow member organizations to join other financial networks, such as WOCCU's IRnet, which has resulted in the two largest credit unions in Mexico, Caja Popular Mexicana and Caja Libertad, deciding not to join La Red. Another concern voiced by several branch managers with CPM and Caja Libertad is that Bansefi, rather than supporting the credit union industry as was originally intended, actually is focused on competing with and even subverting "rival" cooperatives. When asked about Bansefi and La Red, several Caja Popular clients responded with comments such as "they're not trustworthy," and "they charge way too much." Privately, Carrasco admitted to Econoff that Bansefi was suffering from public relations problems issues in 2005 concerning suspected financial mismanagement and malfeasance. In addition, Carrasco also mentioned that Bansefi and La Red are priorities for the Fox administration; the incoming administration may not be as supportive.

THE TRADITIONAL BANKING SECTOR

¶13. (SBU) The traditional banking sector is also targeting the remittance market, aggressively leveraging partnerships with U.S.-based banks to offer convenient transaction services to account holders on both sides of the border. Armando Albores, Regional Director of Banamex in the state of Michoacan, explained to Econoff that more effectively penetrating the remittance market is a top priority. Banamex is cooperating with Citibank, their parent company, to offer low-cost wire transfers (five dollars per transaction) between U.S. and Mexican account holders. While stating the Banamex was a "financial institution for all," Albores

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admitted that the cost of opening a branch in a community with less than 30,000 residents was prohibitive, thereby restricting coverage where many of Mexico's remittance recipients live. (According to the National Institute of Statistics, 35-40 percent of the population lives in communities smaller than 30,000 residents).

¶14. (SBU) Attempting to overcome their poor reputation among many in rural Mexico, some banks are offering services that do not require opening an account. Juan Lavalley of HSBC described a new program which offers a debit/credit card to anyone (not only account holders) receiving remittance funds. Lavalley informed Econoff that while HSBC will not reap a large amount of revenue from this program, its value lies in tracking recipients' spending habits, in order to market additional services to this growing sector in the future. Realizing that migrants' reluctance to frequent banks in the U.S. is also an important prohibitive factor, HSBC is utilizing outreach programs in areas of high migrant populations. There are clear opportunities for the

traditional banks, especially as more migrants begin to utilize banking services in the U.S. Due to a limited client base, however, the banking sector may not be an huge driver of economic growth in Mexico's rural areas in the near future.

NEW GOVERNMENT PROGRAMS

¶15. (SBU) The issue of utilizing remittance income to spur rural economic development has been a central issue for the state government of Michoacan for a considerable period of time, given the state's position as the remittance leader of Mexico. In 1990, Michoacan became the first state to create an Office of Migrant Affairs (there are now equivalent offices in 26 of 32 states), which is tasked with providing a variety of services to migrants, such as notarial services. Considering accessibility to low-cost electronic transfers in rural areas as a humanitarian and social issue as well as an economic one, the Office of Migrant Affairs initiated the first government subsidized financial transfer program in Nahuatzen, a small, underserved farming community in northern Michoacan, in January, 2006. Alejandra Contreras, director of remittance services in the Office of Migrant Affairs, explained to Econoff that this pilot program provides a platform for migrants in the Washington, DC area to make a transfer to a government operated cashier in Nahuatzen for a flat fee of three dollars, far below the average cost. Contreras also stated that the program was just beginning but so far had exceeded all of its benchmarks, and that her office was considering opening two additional branches by the end of the year. However, some view the concrete effects of such a program as being limited, while potentially undercutting private financial institutions and being counterproductive in the long-term. Regardless, this program illustrates that ensuring low-cost financial services and encouraging subsequent economic development in rural areas is an important issue for local and state policy makers.

COMMENT

¶16. (SBU) The challenge of ensuring access to financial services in rural areas in order to harness the incredible economic power of remittances will be one of Mexico's biggest economic and social challenges in the immediate future. While there are a number of positive trends, such as the increased coverage and competency of cooperatives in underserved areas, new programs by banks to attract migrants and their families, and greater attention to this issue by local and state governments, many obstacles remain. While credit union chains such as CPM are continuing to expand and recruit clients, it will take time (and marketing finesse) to overcome a strong reluctance in many areas to utilize financial services. In addition, many of the financial products obtained are used for basic daily consumption, instead of long-term economic investment. Although new services offered by the banking sector should enable less expensive, more convenient financial transactions, many of these services will probably still be restricted to a relatively small percentage of the population in the near term. With the amount of remittance income likely to continue to grow at a strong rate, some economic development should occur in many rural areas. However, this growth will probably occur at a slower rate than could be

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expected given the explosion of remittance income to Michoacan and Mexico.

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